DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS:01-0297; 01-0298
Gross Retail Tax
For the Tax Years 1999 and 2000

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ISSUES

I. Applicability of the State's Gross Retail (Sales) Tax to the Sale of Taxpayer's Coupon Books.

Authority: IC 6-2.5-2-1; IC 6-2.5-4-1; IC 6-2.5-4-1(b): IC 6-2.5-4-13; IC 6-2.5-5 et seq.; Maurer v. Indiana Dept. of State Revenue, 607 N.E.2d 985 (Ind. Tax Ct. 1993); Monarch Beverage Co. v. Ind. Dept. of State Revenue, 589 N.E.2d 1209 (Ind. Tax. Ct. 1992); 45 IAC 2.2-2-2.

Taxpayer argues that sales of its promotional coupon books are not subject to the state's gross retail tax.

II. Imposition of Use Tax on Taxpayer's Free Coupon Books.

Authority: IC 6-2.5-3-1(a); IC 6-2.5-3-2(a); 45 IAC 2.2-3-1; 45 IAC 2.2-3-4.

Taxpayer argues that the purchase price of its free coupon books is not subject to the state's use tax.

III. Prospective Treatment of Taxpayer's Cumulative Gross Retail Tax Liability.

Authority**:** IC 6-8.1-3-3; IC 6-8.1-3-3(b); City Securities Corp. v. Dept. of State Revenue, 704 N.E.2d 1122 (Ind. Tax Ct. 1998); West Publishing Co. v. Indiana Dept. of Revenue, 524 N.E.2d 1329 (Ind. Tax Ct. 1988); 45 IAC 15-3-2(d)(1), (e); 45 IAC 15-3-2(d)(3); 45 IAC 15-3-2(e).

If the Department determines that sales of its coupon books is subject to the gross retail tax and that it should have self-assessed use tax on the price it paid for the free coupon books, taxpayer maintains that it is entitled to prospective treatment of those determinations.

STATEMENT OF FACTS

Taxpayers are two distinct corporate entities one of which is a "spin-off" of the other. The two entities were separately assessed additional sales and use tax. The two entities chose to file a joint-protest, and – for the sake of simplicity and clarity – are addressed simply as "taxpayer" within this Letter of Findings.

Coupon Books Offered For Sale: Taxpayer prints and sells books which consist entirely of promotional coupons. Taxpayer sells some of the books directly to consumers and sells some books for resale. The ultimate purchaser then uses the promotional coupons – during the term in which the coupons remain valid – to obtain merchandise at a reduced price.

Taxpayer arranges with various merchants obtaining permission to include the merchants' coupons in the coupon book. The merchants do not pay taxpayer to have their coupons included in the book. Taxpayer does not pay the merchants to secure permission to include the merchants' coupons. Rather, taxpayer obtains permission to include the merchants' coupons in the book, the merchants supply taxpayer with appropriate commercial artwork, the merchants specify the content and terms of each coupon, and taxpayer prints and binds the accumulated coupons. The "face" value of the various coupons substantially exceeds in value the amount the consumer paid to purchase the book.

The taxpayer sells the promotional books by various means. Taxpayer operates a telemarketing service; taxpayer operates kiosks in shopping malls; taxpayer has a limited number of over-the-counter sales at their main office. In addition to the direct sales, taxpayer sells the coupon books to various businesses for their own use as promotional items, incentives, and gifts. Taxpayer sells some of the coupon books to not-for-profit organizations at a discounted price. The not-for-profit organizations then sell the coupon books at their face value and retain the profit for their own purposes.

The audit determined that taxpayer's direct sales of the coupon books were transfers of tangible personal property subject to the gross retail tax. Accordingly, the audit determined that taxpayer was liable for unpaid *sales* tax.

Free Coupon Books: In addition, taxpayer – under its separate operating identity – prints and distributes free coupon books entirely distinct from the books previously described. These particular coupon books were not sold but were mailed free of charge to potential customers. Taxpayer solicited various merchants to purchase pages in the books. The merchants purchased pages in order to offer discount coupons to the ultimate recipients of the free coupon books. After taxpayer sold all the pages in its free coupon book, it arranged for the printing of the book. During the time period considered by the audit, taxpayer arranged with an out-of-state printer for the production of the free coupon books. After the out-of-state printer completed production of the free coupon books, the books were delivered to an out-of-state mailing service. The mailing service then addressed and mailed the books to targeted geographical areas within Indiana. The taxpayer did not pay sales tax on the printed material and did not self-assess Indiana use tax on the free coupon books. The audit determined that taxpayer should have self-assessed use tax on the price taxpayer paid for the free coupon books consumed within the state.

The taxpayer protested both the sales and use tax determinations, an administrative hearing was held, and this Letter of Findings follows.

DISCUSSION

I. Applicability of the State's Gross Retail (Sales) Tax to the Sale of Taxpayer's Coupon Books.

Under IC 6-2.5-2-1, Indiana imposes a gross retail (sales) tax on retail transactions made within the state. A retail transaction, the pre-requisite to the imposition of the sales tax, is defined as the transfer, in the ordinary course of business, of tangible personal property for consideration. IC 6-2.5-4-1(b).

45 IAC 2.2-2-2 imposes on "retail merchants" the responsibility for collecting sales tax. The regulation states in relevant part that a "retail merchant, acting as an agent for the state of Indiana must collect the tax."

IC 6-2.5-4-1 defines "retail merchants" responsible for collecting sales tax. The statute defines a "retail merchant" as follows:

> (a) A person is a retail merchant making a retail transaction when he engages in selling at retail.
>
> (b) A person is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he:
>
> > (1) acquires tangible personal property for the purpose of resale; and
> > (2) transfers that property to another for consideration.

It is not disputed that taxpayer arranges for the preparation, printing, and assembly of the coupon books. It is not disputed that taxpayer enters into transactions for the sale of the coupon books. However, taxpayer contends that the coupon books do not represent "tangible personal property." According to taxpayer, the coupon books represent an intangible right to acquire property and services from the participating merchants.

To that end, taxpayer argues that the coupon books are analogous to raffle tickets which the Indiana Tax Court, in Maurer v. Indiana Dept. of State Revenue, 607 N.E.2d 985 (Ind. Tax Ct. 1993), found were not subject to the state's gross retail tax. The court held that, "Raffle tickets are evidence of a right to claim a prize if a contingency occurs; they are not tangible personal property." Id. at 989.

However, taxpayer is not selling the coupon book purchasers an undifferentiated random opportunity to win merchandise. Rather, the coupon books themselves possess an inherent, assured value to the individual purchasers. For example, the purchaser acquires one of taxpayer's

booklets that contains a discount restaurant coupon. The coupon allows the purchaser to obtain a meal, normally costing ten dollars, for six dollars. There is no contingency in operation to determine whether or not the coupon does or does not have value because, when the consumer purchased the coupon book, he purchased a sure and certain 40 percent – albeit discounted – share of the restaurant's ten-dollar meal. When the restaurateur charges the consumer for the ten-dollar meal, the restaurateur collects six dollars together with sales tax on that six dollars. Under taxpayer's proposed scenario, the consumer obtains 40 percent of the meal tax-free.

Alternatively, taxpayer argues that the purchase of coupon booklets is similar to the purchase of a gift certificate. When a retail gift certificate is purchased, no sales tax is assessed because the merchant receives no profit and no "retail transaction" occurs at the time the consumer acquires the gift certificate. Rather, the imposition of the tax is deferred until the time that the gift certificate is redeemed in exchange for tangible personal property because that is the point where the "retail transaction" occurs and that is the point where the merchant receives profit attributable to that transaction. However, unlike a gift certificate, no sales tax is ever imposed upon the value represented by the individual coupons. Unlike a gift certificate, there is no retail transaction subject to sales tax when the customer redeems the coupon. The customer merely receives the right to purchase an item at a discount. Sales tax is only charged on the reduced value of the item purchased.

"The essence of a sale is the transfer of title to property for consideration." Maurer 607 N.E.2d at 989. *See also* Monarch Beverage Co. v. Ind. Dept. of State Revenue, 589 N.E.2d 1209, 1213 (Ind. Tax. Ct. 1992). Plainly, taxpayer is a "retail merchant" entering into retail transactions – upon which taxpayer receives a profit – for the transfer of tangible personal property possessing an inherent and assured value. Absent any indication that the sale of the coupon books falls into any one of the exemptions under IC 6-2.5-5 et seq., sales of the coupons books are subject to the state's gross retail tax.

FINDING

Taxpayer's protest is respectfully denied.

II. Imposition of Use Tax on Taxpayer's Free Coupon Books.

Taxpayer argues that the audit erred in assessing use tax on the purchase price it paid for the free coupon books consumed within Indiana.

IC 6-2.5-3-2(a) imposes "[a]n excise tax, known as the use tax . . . on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction." *See also* 45 IAC 2.2-3-4. IC 6-2.5-3-1(a) in turn defines "use" as the "exercise of any right or power of ownership over tangible personal property." *See also* 45 IAC 2.2-3-1.

Taxpayer's acquisition of the free coupon books falls within the purview of the state's use tax scheme. Taxpayer acquired the coupon books as tangible personal property from the out-of-state printer by means of a retail transaction. Taxpayer exercised its ownership over the free coupon books on two occasions; when taxpayer directed the out-of-state printer to deliver the books to the out-of-state mailing service and when it instructed the out-of-state mailing service to then deliver the books to the ultimate Indiana recipients. The free coupon books were used or consumed within the state because the books were directed at, shipped to, and received by targeted Indiana recipients.

Accordingly, the purchase price of the free coupon books delivered to Indiana recipients was properly subject to imposition of the use tax under IC 6-2.5-3-2. That the tangible personal property at issue was prepared and shipped by out-of-state vendors is an irrelevancy under the IC 6-2.5-3-2(a).

FINDING

Taxpayer's protest is respectfully denied.

III. Prospective Treatment of Taxpayer's Cumulative Gross Retail Tax Liability.

Alternative to its primary arguments, taxpayer argues that it is entitled to prospective treatment of the Department's determination that sales of the coupon books were subject to the gross retail tax and the determination that taxpayer's consumption of the free coupon books was subject to the use tax. Taxpayer bases its argument on a letter received from the Department indicating that the sales of the coupon books were not subject to sales tax. The letter dated March 19, 1987, reads in part as follows:

> In response to your question regarding the taxability of coupon book sales, the Department finds that the coupon books are not subject to the Indiana Gross Retail sales Tax. However, when individual coupons from the coupon books are redeemed for the purchase of tangible personal property, sales tax would be collected on the transaction.

Taxpayer maintains that it operated its business in good faith and in reliance upon the correspondence received from the Department.

Under IC 6-8.1-3-3, the Department of Revenue is without authority to reinterpret a taxpayer's tax liability without promulgating and publishing a regulation giving taxpayer notice of that reinterpretation. IC 6-8.1-3-3(b) states that "[n]o change in the department's interpretation of a listed tax may take effect before the date the change is (1) adopted in a rule under this section or (2) published in the Indiana Register . . . ."

In City Securities Corp. v. Dept. of State Revenue, 704 N.E.2d 1122 (Ind. Tax Ct. 1998), plaintiff taxpayer argued that the Department could not impose gross income tax on the grain realized from the sale of tax-exempt bonds, because that gain had been treated as exempt for 42

years. Id. at 1128. Plaintiff taxpayer argued that, in the absence of a new rule or regulation, the Department's assessment of gross income taxes against the gain realized from the sale of the tax-exempt bonds was invalid. Id. at 1129. The Tax Court found that – despite the intervening adoption of regulations to the contrary – the Department could not impose the additional taxes when the Department had permitted plaintiff taxpayer to claim an exemption from the taxes subsequent to the adoption of the intervening regulations. Id. Nevertheless, the Tax Court also held that plaintiff taxpayer, having been placed on notice of its additional tax liability, was responsible for paying the tax on a prospective basis. Id.

However, in West Publishing Co. v. Indiana Dept. of Revenue, 524 N.E.2d 1329 (Ind. Tax Ct. 1988), the tax court held that respondent Department was not estopped from assessing state income taxes based upon a letter respondent Department had previously issued to petitioner taxpayer. Id. at 1334. The West letter was prepared by respondent Department after petitioner taxpayer had replied to respondent Department's request for a detailed description of petitioner taxpayer's business activities in Indiana. Id. at 1331. Petitioner taxpayer argued that the letter, written by one of respondent Department's tax examiners, stated that petitioner taxpayer bore no state income tax liability because respondent taxpayer's activities within the state were limited to the solicitation of sales. Id. at 1333. The tax court disagreed with petitioner taxpayer's contention finding that the "letter does not purport to state that [petitioner taxpayer] bore no tax liability." Id. Instead, the tax court found that "[i]t is true that the letter *could* be read as a statement that [petitioner taxpayer] was not liable, but the mere *possibility* that the Department made such a representation is not, in this court's view, sufficient to create estoppel." Id. (*Emphasis added*).

The West letter directed to petitioner taxpayer read as follows:

> This letter is in acknowledgement of your reply to my correspondence of March 28, 1979. The information which you have submitted has proved to be a sufficient answer to the question raised in my previous correspondence. I would like to thank you for your cooperation in this matter. Id.

The tax court held that petitioner taxpayer was precluded from asserting the estoppel argument, based upon the representations contained within the ambiguous letter, because – inter alia – there was no evidence that petitioner had changed its position in reliance upon those representations. Id. at 1334.

A particular Indiana taxpayer is entitled to place its reliance upon a Department ruling "based on a particular situation which may affect the tax liability of the taxpayer . . . ." 45 IAC 15-3-2(d)(3). The Department will issue advisory letters to individual taxpayers, some of which will be binding upon the Department and some of which will not bind the Department. 45 IAC 15-3-2(e). When an individual taxpayer directs a written inquiry to the Department, describing in full the factual circumstances surrounding a particular transaction and seeking advice as to the tax consequences of that particular transaction, then "[a]ll such rulings issued will be binding provided that all of the facts described in obtaining the ruling are true and accurate. Any misstatement of material fact or information will void the ruling." Id.

Taxpayer's March 19, 1987, Department letter is not analogous to the enigmatic West letter petitioner taxpayer had received from the Department and more closely resembles a written ruling described in 45 IAC 15-3-2(e). Unlike petitioner taxpayer's letter in West, taxpayer's 1987 letter clearly indicated that the Department had considered the nature and object of the tax. Unlike petitioner taxpayer's letter in West, taxpayer's 1987 letter, specifically indicated that taxpayer was *not* subject to the tax. Unlike petitioner taxpayer's letter in West, taxpayer's letter indicated that taxpayer directed a particularized question to the Department seeking advice concerning the taxability of a specific transaction – taxpayer's sales of its coupon books.

Based upon the information now available, the Department concludes that taxpayer's 1987 letter was the result of a specific inquiry, in which taxpayer sought advice as to the tax consequences of a particular transaction. 45 IAC 15-3-2(e). Therefore, taxpayer's March 19, 1987 letter has all the indicia of a written ruling as described in 45 IAC 15-3-2(d)(1), (e), upon which taxpayer was similarly entitled to place its reliance. Because there is no indication that the circumstances surrounding nature or sale of taxpayer's coupon books have changed since 1987, that the facts taxpayer presented to the Department were inaccurate, or that taxpayer in any way misstated the material facts surrounding the coupon book sales, taxpayer could reasonably have expected that the 1987 letter would bind the Department until the Department made a specific determination to the contrary. *See* Id.

Accordingly, for purposes of the assessment of the gross retail tax on the *sales* of its coupon books, taxpayer is in the same position as petitioner taxpayer in City Securities and is entitled to prospective treatment of the determination that sales of the coupon books are subject to the state's gross retail tax. The Department, in language subject to no ambiguity, gave notice to the taxpayer that its coupon books sales fell outside the purview of the tax. There is no evidence that, prior to the audit here at issue, taxpayer was given any notice of a change in the Department's position. There is no evidence that the taxpayer operated in other than good faith in continuing to rely on the Department's position as set out in the 1987 letter. There is no indication that factual setting surrounding the sale of the coupon books has in any way altered during the intervening years.

Therefore – based upon the Department's long acquiescence to the conclusions set out in the 1987 letter and the taxpayer's continued reliance on that same letter – for purposes of the gross retail tax assessment made against the *sales* of its coupon books, taxpayer is entitled to the same treatment afforded petitioner taxpayer in City Securities when the court stated that, "beginning with the first full tax year after the issuance of this opinion, [taxpayer] is considered to have notice of the Department change in policy." City Securities 704 N.E.2d at 1129. In taxpayer's own particular circumstances, taxpayer is considered to have received "notice" of the Department's "change in policy" during June of 2001 – the point at which the original audit report was completed.

However, taxpayer is not entitled to similar prospective treatment on the *use* tax assessment made against the consumption of the free coupon books within the state. The 1987 Department letter is straightforward; "In response to your question regarding the taxability of coupon book *sales*, the Department finds that the coupon books are not subject to the Indiana Gross Retail *Sales* tax." (*Emphasis added*). Although the taxpayer may have had a good faith belief that the

determination contained within the 1987 letter could be applied to resolve use tax issues, it was plainly not entitled to do so. The facts surrounding the preparation and ultimate sales of its coupon books were distinct from the circumstances surrounding the acquisition of the free coupon books intended for consumption within the state. For purposes of determining its *use* tax liability, the 1987 letter was not a written ruling upon which the taxpayer was entitled to place its reliance or a written ruling which in any way bound the Department. *See* 45 IAC 15-3-2(e). Accordingly, taxpayer was not entitled to conclude that it could acquire coupon books destined for free distribution (consumption) within the state without self-assessing use tax.

FINDING

Taxpayer's protest is sustained in part and denied in part.

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